

Strategic alignment between competitive strategy and dynamic capability: conceptual framework and hypothesis development

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Strategic alignment between competitive strategy and dynamic capability: conceptual framework and hypothesis development¹

Short title: Strategic alignment between competitive strategy and dynamic capability

Summary

We suggest that in e-business, competitive strategies and dynamic capabilities should be aligned, as this strategic alignment may enable them to create superior value for their stakeholders.

Article key points:

- Not all e-businesses with planned competitive strategies outperform their competitors, especially when they underscore the significance of dynamic capabilities in their competition.
- Successful development and implementation of competitive strategies depend on a proper deployment of dynamic capabilities.
- No single competitive strategy could create superior value; rather, value is obtained through the capacity of an e-business to align its competitive position regarding its internal possessions.
- We expect that as the alignment between competitive strategies and dynamic capabilities increases, the e-business value creation increases in terms of novelty, lock-in, complementarities and efficiency.

Introduction

Due to the nature of competition over the Internet, e-businesses must make their strategic decisions quickly to respond to high-level technological and market changes (Sher and Lee, 2004). The results of these quick responses are not always desirable, and it is sometimes damaging to a firm's performance. This problem arises since the strategic decisions are not usually made in 'strategic alignment' with a firm's external and internal characteristics.

¹ JEL classification codes: L100, L250, M130, M150.

Strategic alignment is a fit between a firm's strategy and its internal and external factors (Venkatraman and Camillus, 1984). The significance of strategic alignment to managers has sparked the interest of scholars in the field and contributed to a considerable increase in research over the past two decades. Strategic alignment is rooted in Configuration theory (Miles and Snow, 1978). This theory is one of the modern variations of Contingency theory (Miller *et al.*, 1984). According to Contingency theory, strategy is not a universal concept, but a contingent factor (Donaldson, 2006), which must be fitted into its context, both internal and external (Acur *et al.*, 2012) in order to enhance performance (Bergeron *et al.*, 2004). This fit is crucial, as it needs to support competitive strategies within a firm. In fact, it can aid organizations in acquisition and development of resources and capabilities, which fit into the firm's competitive position (Rondinelli *et al.*, 2001).

The significance of strategic alignment in an e-business context has been devoted to the fit between e-business competitive strategies and internal factors, particularly capabilities (Raymond and Bergeron, 2008). Capabilities are the firm's most enduring and reliable bases in any competitive strategy development (Grant, 1991). They are the building blocks of RBT (Valentin, 2001). RBT is one of the main strategic management approaches (Priem and Butler, 2001). This theory suggests that organizations enhance their performance if they develop and implement their competitive strategies based upon their capabilities (Barney, 2001).

Nevertheless, due to the inherently dynamic nature of strategic alignment (Henderson and Venkatraman 1993), a particular type of capabilities, namely dynamic capabilities, has been advocated as a necessary part of any strategic alignment (Kearns and Lederer 2003). Dynamic capability is "the firm's ability to integrate, build and reconfigure internal and external competences to address rapidly changing environments" (Teece *et al.*, 1997). The significant role of dynamic capabilities in developing value-creating strategies is undeniable (Eisenhardt and Martin, 2000). Hence, the strategic alignment of dynamic capabilities with competitive strategies is important. It is suggested that e-businesses whose competitive strategies and dynamic capabilities are aligned may be less vulnerable to environmental changes. Therefore, they should have a competitive position in the market (Kearns and Lederer, 2003), as they might be better value creators for their stockholders.

Although several prior studies have examined strategic alignment, it is subject to several critical limitations. First, there are still some questions of whether - and how - strategic alignment creates value (Tallon, 2011). Value is defined as the non-financial aspects of performance measurement from the stockholders' view (Amit and Zott, 2001). Almost all the existing research (except Boonstra *et al.*, 2011), has examined the impact of alignment on financial measures of performance, while value has been suggested as a better predictor to study the impact of capabilities on a firm's overall outcomes (Soto Acosta *et al.*, 2011). In this respect, Amit and Zott (2001) suggest that e-businesses may create value in terms of novelty (innovative offerings), lock-in (retaining partners), complementarities (complementary offerings) and efficiency (mainly through cost reduction).

Second, a few studies have postulated the alignment of competitive strategies and capabilities (e.g., Gonzalez-Benito and ISuarez-Gonzalez, 2010); however, there is almost no systematic research to consider dynamic capabilities, and in an e-business context in particular. In fact, much of the existing literature in this regard has employed a traditional 'reductionistic approach' in which a linear, often bivariate association has been found to exist between dynamic capabilities and performance (e.g., Drnevich and Kriauciunas 2011). However, a holistic approach of strategic alignment has a greater power to explain the complex interrelationship between different constructs (Venkatraman and Prescott, 1990). This approach is able to capture the co-variation (all the interactions and synergies) between competitive strategies and dynamic capabilities and their resulting impact on value. Hence, these constructs are not examined in isolation, as this would result in ignoring their configuration and its influence on value in a comprehensive perspective.

In view of the aforementioned limitations, we aim to provide a systematic investigation into the strategic alignment between competitive strategies and dynamic capabilities and its resulting impact on e-business value sources. To achieve this aim, our objectives are twofold: 1) understand to what extent strategic alignment exists in e-businesses and 2) explore how strategic alignment creates value in e-businesses. We conceptualize the research objectives through a research framework and its five correspondent hypotheses, which are all informed by several organizational theories and frameworks, such as Strategic alignment model (Henderson and Venkatraman, 1993), RBT

(Wernerfelt, 1984), Configuration theory (Meyer *et al.*, 1993) and e-business value creation framework (Amit and Zott, 2001).

Theoretical foundation of the study

As mentioned earlier, we develop this paper based on two theories of Configuration and RBT.

Configuration theory

Configuration theory is able to simplify the investigation between the multi-dimensional constructs of competitive strategies and dynamic capabilities (Sabherwal and Chan, 2001). Configuration refers to common alignments among elements (Miller, 1996). It is able to conceptualize the association among various contingency constructs, which commonly occur together in a context (Meyer *et al.*, 1993). This theory can work better than simpler contingency theory, since the ‘strategic fit of a firm’s competitive strategies and dynamic capabilities’ can be a better predictor of value generation (Chan *et al.*, 1997). By applying this theory, these two constructs are examined in a holistic approach, rather a reductionistic approach. Hence, this theory will enable us to examine which configuration of these two constructs may enhance e-business value creation.

Resource Based Theory (RBT)

This theory simply emphasizes the idea that organizations must be seen as a bundle of resources and capabilities to create value and therefore gain competitive advantage (Barney, 1991). RBT has also been extended by Grant (1991) to encompass competitive strategy. According to Grant, RBT links competitive strategies and capabilities to value creation. He posits that not only do capabilities need to be considered as the base to develop competitive strategies, but also that capabilities are renewed and maintained by strategies. Hence, RBT is important to understand the reciprocal relationship between these two constructs, and therefore to assess the alignment between them.

From configuration theory perspective, RBT argues that value may stem from strategic alignment, when it presents a complex selection and configuration of capabilities that are heterogeneous across firms and imperfectly imitable (Barney, 1991). Thus, organizations may generate value if there is a match between their capabilities, as the

building blocks of RBT, and their competitive strategies. In this paper, we employ RBT and configuration theory together to describe how an e-business creates value by aligning dynamic capabilities to competitive strategies. Thus, based on these two theories, we propose our conceptual framework in the next section.

A strategic alignment conceptual framework

We demonstrate the conceptual framework of this study is Figure 1. This framework suggests that successful development and implementation of competitive strategies depend on a proper deployment of dynamic capabilities. Furthermore, it evokes that no single competitive strategy could create superior value. Rather, value is obtained through the capacity of an e-business to align its competitive position regarding its internal possessions. In order to propose the related hypotheses, we divide this section into two main parts. First, we present a brief review on different parts of the framework. Second, the correspondent hypotheses are developed to conceptualize the ‘co-vary’ between competitive strategies and dynamic capabilities (hypothesis 1) and its resulting impact on four sources of e-business value (hypothesis 2-5).

<Insert Figure 1 about here>

A review on key aspects of the framework

Competitive strategies

Porter’s (1980) framework of generic strategies is an appropriate typology to study e-business competitive strategies, as it has received the highest research attention than other typologies (Koo *et al.*, 2004). Moreover, several authors (e.g., Kim *et al.*, 2004a; Kim *et al.*, 2004b) have admitted its applicability in an e-business context. However, this framework has been modified in several studies in an e-business context. For instance, Kim *et al.* (2004a) believe that ‘focus’, as a necessary condition for any e-business to become successful, is no longer a strategic option, but a competitive imperative. Furthermore, some scholars have extended Porter’s strategies, particularly ‘differentiation’, in an e-business context (e.g., Plant, 2000). The two most important ones are ‘product-service’ and ‘marketing’ (Miller, 1988). Product-service differentiation refers to offering innovative and most up-to-date products and services to

customers in terms of quality, efficiency, and design (Miller, 1986). Marketing differentiation implies creating a unique image for a product via advertising, marketing, and prestige pricing. Thus, we consider three strategies of cost leadership, product-service differentiation, and marketing differentiation in our proposed conceptual framework.

Dynamic Capabilities

According to Zhu and Kraemer (2002), dynamic capabilities “reflect a company's strategic initiatives to use the Internet to share information, facilitate transactions, improve customer services, and strengthen supplier integration.” By using the Internet, e-business dynamic capabilities are able to meet the major strategic issues facing firms to be innovative, flexible, and quick respondent; particularly when the rate of changes in the electronic marketplace is high and therefore, any market prediction is difficult (Sher and Lee, 2004).

Several authors have attempted to classify dynamic capabilities across organizations. For instance, Teece and Pisano (1994) argue that dynamic capabilities can be classified into three groups of ‘integration’, ‘learning’, and ‘reconfiguration and transforming’. Having evaluated the dynamic capabilities’ typologies and frameworks, four processes of sensing, learning, integrating and coordinating, proposed by Pavlou and El Sawy (2011) have been found which cover all the existing types of dynamic capabilities in the literature. This category can aid managers and strategists to organize and harness disciplinary knowledge to understand how organizations can create value (Teece, 2011) with regard to their strategic alignment. These four dynamic capabilities are outlined as follows.

Sensing is the ability of firms to understand, create and interpret opportunities in the market (Schilke and Goerzen, 2010) and calibrate the needs for change (Teece *et al.*, 1997). Learning is the ability of firms to address the opportunities, identified by sensing capability through proposing new products and services (Teece, 2007). In fact, by revamping operational capabilities, learning enables firms to create knowledge (Hurley and Hult, 1998). Integrating enables firms to absorb and embed new knowledge from external resources into the new operational capabilities ((Lawson, 2001). In fact, it attempts to combine individual knowledge, acquired by learning capability, into a firm’s

operational capabilities by creating a shared understanding and collective sense-making ((Pavlou and El Sawy, 2011). Coordinating is the ability of firms to govern activities, resources, and tasks into the new operational capabilities (Pavlou and El Sawy, 2011). This is followed by coordinating and orchestrating the interdependencies among them (Tarafdar and Gordon, 2007).

Strategic alignment of competitive strategies and dynamic capabilities

The fundamental assumption of strategic alignment is that firm performance may not be enhanced, if competitive strategy misfit a firm's contexts (Bergeron *et al.*, 2004). In fact, strategic alignment has adapted a 'holistic' perspective, which is in contrast to the traditional 'reductionistic' approach. According to Meyer *et al.* (1993) reductionism is defined as "an approach whereby researchers seek to understand the behaviour of a social entity by separately analysing its constituent parts"; whereas, a holistic approach of strategic alignment is able to capture all the interactions among various constructs (Fink 2011). In this regard, while there is ample research (e.g., Mithas *et al.*, 2011; Kim *et al.*, 2011) evidence on the various reductionistic relationships among competitive strategies, capabilities and performance (including value), there are very few studies that have examined the relationship among these constructs through a holistic approach of alignment. To the best of our knowledge, there are only three studies (see Raymond and Bergeron, 2008; Gonzalez-Benito and ISuarez-Gonzalez, 2010; McLaren *et al.*, 2011) that examine the holistic approach of alignment between competitive strategies and a firm's capabilities and their impact on performance. We have understood from these studies that alignment has never been used for dynamic capabilities in a holistic view with competitive strategies in an e-business context, which is the focus of this paper.

In light of the shortcomings of the existing literature, this paper proposes that e-business may enhance firm performance through value creation to the extent that it would be in alignment with competitive strategies and dynamic capabilities, both in 'formulation' and 'implementation' strategy phases (Venkatraman and Camillus, 1984). In fact, we suggest strategic alignment to enhance organizational ability to predict under which circumstances it can reach to high e-business value.

E-business value creation

Strategic alignment must significantly contribute to performance (Kearns and Lederer, 2003). However, as value creation is the main objective of an e-business (Yu, 2006), performance measurement in an e-business context must focus on value (Hackney *et al.*, 2004). Similarly, Soto Acosta *et al.* (2011) believe that although examining financial measures of performance seems predominant in the studies, it may not be the most appropriate construct to study the impact of a firm's capabilities on its overall outcomes. They believe that the performance outcomes of all IT and e-business's investment might not be achieved shortly, but perhaps, they might be seen through the value created for a firm's stockholders.

E-business value sources have been investigated in several studies (e.g., Zhu *et al.*, 2004; Zhu and Kraemer, 2005). Among these studies, the research of Amit and Zott (2001) has a distinctive exception from others, which makes it more appropriate to be employed in several studies (e.g., Sainio *et al.*, 2011). According to Amit and Zott, performance should be measured through four sources of value: novelty, lock-in, complementarities and efficiency. Novelty is one of the traditional sources of value through innovative provision of new products, services, distribution and marketing channels. Lock-in is enhanced in two main ways: 1) customers who are motivated to repeat their transactions, and 2) partners who are willing to maintain a durable association with the focal firm (Zott and Amit, 2010). Complementarities create value for customers by offering bundles of products, services and distribution channels (Zott and Amit, 2007). Efficiency deals with decreasing cost to provide higher benefits for vendors and customers (Zott and Amit, 2007).

Having reviewed different constructs of the conceptual framework, in the following section we present the related hypotheses to conceptualize the relationships between these variables.

Research hypotheses

Covariation of competitive strategy and dynamic capability

As the review of the literature has so far showed, competitive strategies and dynamic capabilities co-vary, since strategy decisions influence dynamic capabilities and vice

versa. In this context, co-vary implies the interrelationships between these two constructs which is consistence with the concept of alignment (Yarbrough *et al.*, 2011). Henderson and Venkatraman (1993) posit that capabilities may positively contribute to the development of new strategies or supporting current strategies. In an e-business context, Liu et al. (2011) argue that dynamic capabilities should be considered in competitive strategy development to provide an e-business with success. Moreover, the findings suggest that dynamic capabilities are mainly developed to identify and shape opportunities in the market (Helfat and Winter, 2011). In other words, strategic competition over the Internet demands new dynamic capabilities, and these new capabilities might be able to alter the competition rules. Therefore, dynamic capabilities must be kept in alignment with competitive strategies; since without strategy, a firm may not appropriately deal with managing its internal resources, processes and systems, as well as external opportunities and threats (Sirmon and Hitt, 2003). The foregoing arguments seem to propose that:

H1: In an e-business, competitive strategies and dynamic capabilities co-vary.

The impact of the alignment on novelty

Offering highly innovative and tailored products and services to customers, mainly through differentiation strategies, may not be possible, if these competitive strategies could not be supported by a high ability of e-businesses to sense and shape new opportunities in the market. Arguably, competitive strategies may be difficult for competitors to imitate, particularly in electronic markets, if these strategies are underpinned by firm-specific dynamic capabilities. Taking this line of exploration, Watson et al. (2007) assert that due to an oversupply of products and services, organizations must be innovative to keep their customers satisfied. They claim that failure to be as innovative as competitors may lead the organization to lose its market share, or even collapse. Therefore, e-businesses are successful if they are able to extract new ideas from customers, as the main sources of innovation by using new Internet-based technologies; particularly, we expect to find those e-businesses adopted product-service strategy to make a great level of novelty value. The reason is that they focus on identifying the key attributes of products and services for better responding to

customers' needs. Therefore, to deliver differentiated business value, as one of the main objectives of an e-business (Hooft and Stegwee, 2001), having a differentiated business configuration is required (Teece, 2010). In light of this argument, we hypothesize that:

H2a: There is a positive association between competitive strategies-dynamic capabilities alignment and e-business value creation in terms of novelty.

The impact of the alignment on lock-in

The key objective of those e-businesses pursuing lock-in value is to develop long-term relationships with their partners including buyers and sellers (Amit and Zott, 2001). We posit that this goal may not be perfectly accessible, if e-businesses do not develop their competitive strategies properly according to their market position, and second, their planned competitive strategies are not fostered by their dynamic capabilities. Strategic alignment may help e-businesses to make a trade-off between costs and benefits in the market to maintain their partners.

The ability to retain customers requires a flexibility to meet their needs; hence, it must be followed based on a dynamic process. Those e-businesses with a high level of dynamic capabilities should be more able to respond to the dynamic process of sensing the changes in customers' preferences and therefore, prevent their migration. In this regard, Kim et al. (2004b, p.23) assert that "firms that reduce customer search costs, engender trust, and offer products, services, and online experiences tailored to their users' needs are likely to elicit initial and repeat purchases". Thus, what is crucial to activate actual buying transaction in electronic marketplace, is using the Internet to reduce the costs and provide a high level of satisfaction and convenience for customers to retain them. Thus, we expect that:

H2b: There is a positive association between competitive strategies-dynamic capabilities alignment and e-business value creation in terms of lock-in.

The impact of the alignment on complementarities

E-businesses can leverage the potential for delivering superior complementarities value by offering their customers bundles of complementary innovative products and services. This leads managers to have a customer perspective to understand exactly what their customers need. We suggest that developing differentiation strategies aligned with the capabilities of firms to identify and respond to customers' needs might be the key message for those e-businesses seeking to obtain a high level of this value source.

One of the main aspects of complementarities in an e-business is offering customers complement channels (Kim and Lim, 1988). Compared to pure players, click-and brick firms may provide greater customer service by offering both online and physical product returns; thus, they should present greater complementarities value (Kim *et al.*, 2004b).

Aside from the significance of sensing and learning dynamic capabilities in generating complementarities, referred above implicitly, integrating and coordinating dynamic capabilities also play crucial roles in this regard. The reason is that an e-business and its customers may not benefit from a range of complementary offerings if there is any conflict in them. Thus, the ability of an e-business to leverage information technologies to integrate and coordinate organizations' resources, processes and systems, is the key to provide integrated and supplementary offerings. Hence, we hypothesize that:

H2c: There is a positive association between competitive strategies-dynamic capabilities alignment and e-business value creation in terms of complementarities.

The impact of the alignment on efficiency

In e-market, customers are more sensitive, demanding, informed and impatient. They look for lower prices, but better service, and efficient processes to benefit exceptional value (Jutla *et al.*, 2001). The Internet aids firms to decrease their cost and take the advantages of a higher level of pricing flexibility, therefore enhancing the efficiency of firms (Kim *et al.*, 2004b). Thus, efficiency is associated to profitability, effectiveness and nonfinancial goals (Homburg *et al.*, 1999). Lumpkin *et al.* (2002) postulate that cost competitors are more efficient as they have to keep the prices at the lowest possible level to compete in the market. However, they posit that the advantages of this value source can be easily imitated if they are not underpinned by high-level dynamic

capabilities. The reason is that Internet itself is ubiquitous; hence, it might not be the source of value creation. In this regard, Fahy and Hooley (2002) believe that two important issues, namely a firm's capabilities, and competitive strategies can significantly affect a firm's outcomes from the Internet. Thus, those e-businesses who can take the most advantage of the Internet by their dynamic capabilities to find and seize optimal cost-cutting ways are more efficient. This efficiency could be greater, if a firm's competitive strategies and dynamic capabilities are matched together to leverage the Internet and its technologies to become cost efficient. Hence, we hypothesize that:

H2d: There is a positive association between competitive strategies-dynamic capabilities alignment and e-business value creation in terms of efficiency.

Implications and discussion

In reconciling our research findings with previous theoretical and empirical work, this research has a number of contributions.

From a theoretical perspective, the holistic approach of strategic alignment, based on Configuration theory, put forward a valid theoretical foundation on how to achieve value from the fit between competitive strategies and dynamic capabilities. In this regard, we endeavour to provide a deeper understanding of the relationship between Porter's generic strategies (Porter, 1980) and dynamic capabilities and its impact on the e-business value sources (Amit and Zott, 2001). Therefore, it is one of the first attempts from the following perspectives.

First, it theoretically contributes to extend the application of the Configuration theory and the strategic alignment concept in an e-business context. Second, it is one of the first studies, which considers dynamic capabilities in particular, to align them with competitive strategies. Therefore, it may help scholars to understand the significance of dynamic capabilities in strategic alignment. Third, it can contribute to RBT literature by examining how different configurations of dynamic capabilities and competitive strategies may contribute to a high level of value creation in organizations. Fourth, it extends the literature by examining the association of strategic alignment with value creation, as a better predictor to examine the result of competitive strategies-dynamic capabilities alignment.

Second, as a result of implementing this research, first, it will assist managers to answer some of their fundamental questions of whether and how e-business investment creates value; which factors contribute most and which of them are more crucial. Second, managers have little direction from the existing literature that informs them of how to achieve the highest benefits from their dynamic capabilities. In this regard, the present study endeavours to improve managers and strategists' understanding of their 'strategic decisions'; not only based on their dynamic capabilities, but also based upon their expected value creation. Third, managers should note that the use of the proposed conceptual framework requires understanding of its dynamic nature. Hence, ensuring continuous assessment of the fit between competitive strategies and dynamic capabilities is one of the challenges for managers.

Conclusion

We designed this study to propose that e-business may enhance firm performance through value creation to the extent that it would be in alignment with competitive strategies and dynamic capabilities. We attempted to raise exiting awareness on significance of strategic alignment in e-business and its resulting impact on value creation. In so doing, we tried to narrow the existing gaps in the relevant literature on the holistic perspective of four main areas of competitive strategy, dynamic capability, strategic alignment and e-business value. Rooted in Contingency theory and RBT, we proposed a conceptual framework to postulate the relationships between these areas. Five correspondent hypotheses have been proposed to be investigated though future research in e-business market. Findings tied to this initiative will assist managers and strategists on their strategic decisions to achieve their expected value creation.

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Biographical notes

Mona Rashidirad is a PhD student in Strategic Management at Kent Business School, University of Kent, Canterbury, Kent, UK. She is also an associate lecturer in Mathematics and quantitative methods in Centre for English and world languages, University of Kent, UK.

Hamid Salimian is a PhD student in Operations Management at Kent Business School, University of Kent, Canterbury, Kent, UK. He is also a part time teacher in operations management at Kent Business School.